

Discussion on Stock Price Trend of Chinese Dairy Industry

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ABSTRACT

In the first quarter of 2020, the New Year holiday, which should have been a peak sales period due to the outbreak, left dairy companies with a sudden backlog of inventory. As the epidemic was brought under control, businesses resumed work and production, and logistics and transportation were resumed, enabling dairy companies to resume production and sales. The share prices of dairy companies, however, show a double scene of fire and ice on the capital market. In this article, we examine the performance of A-share listed companies in the dairy industry during the COVID-19 period.

Keywords: Stock price, Dairy Industry, China

1. INTRODUCTION

Despite the strict preventive and control measures taken by European countries in general, Newcastle pneumonia continues to spread, with new cases and deaths just outside China reaching record levels. The spread of the disease has been largely contained in China. The Chinese dairy industry has shown more responsibility, synergy, and ability to contribute to the common prosperity of the industry in the face of this new pneumonia epidemic. During the time of the stock market meltdown in the United States, the domestic stock market was also affected, but soon returned to a "healthy" state, especially after the recent stock market performance of the dairy industry, which was up significantly [1]. As investor sentiment increased due to the outbreak of COVID-19, a new coronavirus infection, global stock markets plunged. Moreover, as China is the world's second-largest economy, investors are concerned that the outbreak will have an adverse impact on the global economy.

2. PRICE VOLATILITY OF CHINESE DAIRY COMPANIES DURING COVID-19

2.1. Industry space

China's dairy products grew rapidly between 2005 and 2014, with a compound annual growth rate of 13.9%.

However, after 2014, sales growth slowed, and raw milk prices continued to fall, causing the industry to reach low single-digit growth. Based on a compound growth rate of 4.56% between 2015 and 2019, total dairy products retail sales in 2019 exceeded 400 billion. It is predicted that by 2024 the dairy products market retail sales will exceed \$550 billion [2]. China's per capita milk consumption is still far lower than that of developed countries when compared to the world average. China had a per capita consumption in 2018 of 17.44 kg, while Japan and the United States had per capita consumptions of 38.65 kg and 84.85 kg, respectively. It is evident from this study that there will be a market for 2-5 times more dairy products in China in the future due to the change in consumer habits.

2.2. The industry competition pattern

Currently, the competitive landscape of the industry is fairly stable. It can be divided roughly into three categories based on popularity, size of operation, and strength of organization. Dairy companies with national sales networks, leading revenue levels and market shares represented by Yili, Mengniu, and others. Regional dairy companies, represented by Guangming Dairy, New Dairy, and Sanyuan, which hold a leading position in the key regional markets in which they operate. They provide a valuable complement to the national dairy companies. Lastly, there are local dairy companies that are smaller in scale and usually operate in a single province or city, with

a small market share and limited competitive strength. Yili and Mengniu Dairy form a duopoly of ambient dairy products, while the second tier of companies is more likely to compete with low-temperature products, which are more likely to grow.

2.3. Pasteurized milk/low-temperature dairy products will become a golden track

With increasing consumption levels, residents are increasingly choosing to purchase low-temperature milk (pasteurized milk) products due to their freshness and higher nutritional value, and future growth rates of ambient milk will be less than those of low-temperature milk. In addition, obstacles to the development of fresh milk are gradually being removed from the supply side.

Historically, the uneven distribution of upstream milk sources has been the primary cause of the low proportion of fresh milk in China. This constraint is now being gradually eliminated. The northern regions of Inner Mongolia, Heilongjiang, Hebei, and Xinjiang are the most important milk producers in China, while the economically developed south is the main consumer of fresh milk in China. The dairy industry in the south has built its own farms in recent years and established long-term partnerships with local farmers to increase the self-sufficiency rate of milk sources. The development of cold chain logistics and the expansion of cold storage in the low-temperature storage sector has contributed to the expansion of sales of low-temperature products, and improvements in the pasteurization process have also prolonged the shelf life of fresh milk categories. During the epidemic, the cultivation of online consumption habits was catalyzed, and the rise of fresh food e-commerce platforms such as Daily Fresh helped to boost fresh milk consumption.

3. PRICE VOLATILITY OF CHINESE DAIRY COMPANIES DURING COVID-19

Figure 1 shows the selected dairy company stock prices in February 2020

Sanyuan 600429	4.76	+0.10	+2.15%
Guangming 600597	10.90	+0.53	+5.11%
Yili 600887	29.54	+1.16	+4.09%
Mengniu 02319	30.550	+1.350	+4.62%
H&H 01112	32.000	+0.400	+1.27%
China Feihe 06186	10.060	+0.470	+4.90%

Figure 1 Selected dairy company stock prices in February 2020



Figure 2 Yili (600887) Dairy Annual K-Chart (Stock market chart)

Yili (600887) rose to a higher share price on March 5, 2020, with a high share price of RMB 31.28 and a low share price of RMB 30.22, up or down +1.91%. The company's share price fell to a low on March 16, with a high of RMB 28.25 and a low of RMB 27.05 on that day, up or down a minimum of -3.57%. It had a total market capitalization of RMB173 billion, a net worth of RMB24.50 billion, and a net profit of RMB5.631 billion as of April 2020 [3] (see Figure 2).



Figure 3 Mengniu (02319) Dairy Annual K-Chart

Mengniu (02319) rose to a higher share price on March 5, 2020, with a high share price of RMB29.80 and a low share price of RMB28.70, a gain or loss of 3.5%. The stock dropped to a low share price on March 13, with a high share price of RMB26.95 and a low share price of RMB24.35 on that day, up or down a minimum of -1.11%. As of April 2020, the company had a market capitalization of 105.1 billion, shareholders' equity of 32.52 billion, and net profit of 4.796 billion (Figure 3).

A higher share price was achieved by Zhuangyuan Pasture (002910) on March 25, 2020, with a high share price of RMB12.42 and a low share price of RMB11.55. This represents a -0.66% change in the share price. Share prices fell to a low of RMB9.40 on March 16, with a high share price of RMB9.69 and a low share price of

RMB9.69 on that day, up or down by a minimum of 0.00%. At the time of writing, the total market value is 2.101 billion, the net assets are 1.212 billion, and the net profit is 38.15 million.

China Shengmu (01432) rose to a higher share price on March 10 2020, with a high share price of RMB0.270 and a low share price of RMB0.231, up or down by 11.11%. The share price fell to a low on March 19, with a high share price of RMB0.230 and a low share price of RMB0.188 on that day, up or down by a minimum of -6.52%. The total market capitalization of the company as

of April 2020 was RMB1.353 billion, shareholders' equity was RMB2.294 billion and net profit was -RMB1.145 billion.

The share price of Tianrun Dairy (600419) increased to a higher level on March 5, the highest share price of 12.50 yuan, the lowest share price of 11.74 yuan; up or down +5.03%. The share price fell to a low on March 17, with a high of RMB11.23 and a low of RMB10.52, up or down by -0.63%. As of the date of this writing, the company had a total market value of 3.183 billion, net assets of 1.167 billion, and a net profit of 181 million.



Figure 4 Tianrun Dairy (600597) Dairy Annual K-Chart (Stock market chart)

Tianrun Dairy (600597)'s share price rose to a record high on March 6. The highest share price was 11.75 yuan, the lowest was 11.43 yuan; up or down 1.64%. On March 19, the share price fell to a low, with the highest share price of 10.15 yuan and the lowest of 9.80 yuan; up or down +0.10%. There is a total market value of 13.63 billion, assets of 6.955 billion, and a net profit of 444 million (Figure 4).

In terms of the share prices of the dairy companies mentioned above, it is noteworthy that around March 5, most of the stock prices of dairy companies are higher, reflecting an upward trend.

3.1. Share Price Analysis

The outbreak had a significant impact on the consumer market during the first half of 2020, but it also provided another kind of opportunity.

China Feihe's share price rose by 71.74% in the first half of 2020, allowing it to surpass Mengniu Dairy in terms of market capitalization [4]. In terms of revenue scale, Feihe, which only produces milk powder, is far inferior to Mengniu. The company's high gross margins and rapid revenue growth have led to Feihe's market value reaching nearly 130 billion yuan now, which is 20 billion yuan higher than Mengniu Dairy, however it is still 60 billion yuan short of Yili [5].

Original Ecological Herding, a supplier to three of the largest dairy companies, Feihe, Mengniu and Guangming, saw its share price rise by 57.63% in the first half of 2020, a proportion not seen in raw milk companies. During the same period, raw milk companies Western Herding and Modern Herding's share prices continued to decline, with Modern Herding's share price declining 25%. Dairy industry diversified in the first half of 2020, temporarily escaping the trough and increasing by more than 50%. In the first half of the year, Yili's share price rose by 3.35%, while Mengniu's share price declined by 5.41% [6].

Investors are concerned that the outbreak may affect the global economy, since China is the world's second-largest economy. The majority of Chinese dairy companies are still performing strongly, and their shares are still rising. Obviously, not all of them are rising, and it is mainly the A-shares that are affected, with some dairy stocks actually dropping, including Western Herding.

However, the effect of the outbreak on the market was short-lived. As a result of the outbreak, risk assets have been adjusted downward, reflecting a temporary shock and the impact of risk aversion rather than illustrating a medium to long-term trend in fundamentals.

Furthermore, dairy products for all ages have strong essential attributes for consumers, especially milk powder for infants and young children. This means that

the impact of this outbreak on the share prices of dairy companies will be minimal, and any declines that may occur will be temporary. A long-term value investor's investment is in the economy and the future of the company [7].

When the epidemic was severe, logistics and the inconvenience of online or offline purchases caused a rapid decline in dairy sales, while when the epidemic improved, pre-existing dairy companies were under pressure to stock up and were forced to engage in promotion, reducing the profitability of their products [8].

Nevertheless, it is worthwhile to note that the outside world has generally viewed the dairy industry's performance positively. Guosheng Securities reported in a research note dated 5 January 2021 that the current raw milk price had reached RMB4.18/kg, which is close to the 14-year historical peak of RMB4.27/kg [9]. The milk price is mildly rising according to historical analysis. It is expected that industry leaders will work together to reduce price promotion. Leading profitability and performance elasticity are expected to continue to expand [10].

4. CONCLUSION

In the first half of last year, raw milk prices declined sharply, particularly in the first quarter. However, after the epidemic subsided, domestic dairy and dairy consumption demand rebounded rapidly, and raw milk prices climbed considerably. With the rapid growth in domestic dairy consumption since the New Year, raw milk supplies have been oversupplied. This has caused upstream raw milk prices to increase, as well as dairy product price increases by companies. The renewed prosperity of the dairy industry has affected the secondary market, with a number of dairy stocks showing an upward trend since the second half of 2020.

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